



County of Los Angeles **CHIEF ADMINISTRATIVE OFFICE**

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May 25, 2004

To: Supervisor Don Knabe, Chairman
Supervisor Gloria Molina
Supervisor Yvonne Brathwaite Burke
Supervisor Zev Yaroslavsky
Supervisor Michael D. Antonovich

From: David E. Janssen
Chief Administrative Officer

SACRAMENTO UPDATE

State Budget Update

Special District Property Tax Shift

Under the agreement between the Administration and local governments regarding their contribution to the State budget solution, each level of government was allowed to determine the method of allocating their contribution. Late last week, special districts reversed their initial determination and decided to exempt fire districts from the two-year property tax shift of \$350 million. The exemption for library districts remains unchanged. In order to make up for the loss from exempting fire districts, the contributions of non-enterprise special districts will increase accordingly. The Special District Association has not released a detailed list showing the final shift shares for all special districts.

Legislative Analyst (LAO) Releases Critique of the Local Government Agreement

Yesterday, the LAO released its analysis and critique of the agreement between the Governor and local governments. The LAO, which had summarized its concerns in its analysis of the Governor's May Revision, has now expanded on that analysis and offered the Legislature an alternative.

The Agreement

The agreement between the Governor and local governments consists of four major elements of concern to the LAO:

- For two fiscal years – 2004-05 and 2005-06 – local governments will shift \$1.3 billion of their revenue to schools to help balance the State budget, with counties, cities, and special districts (other than fire and library districts) giving up \$350 million and community redevelopment districts \$250 million each year.
- Counties and cities will swap \$4.1 billion of vehicle license fees for a comparable amount of property taxes (except for the two-year contribution above).
- Local government revenues will be protected through a constitutional amendment to be placed on the ballot in November that will prohibit the State from reducing the rate of the local sales tax, or reallocating any local government's share of revenue from the property tax, sales tax, or vehicle license fees (except for their two-year contribution).
- Unfunded State mandates (except for educational or employee rights or benefits mandates) will sunset automatically and cannot be suspended in the budget. In addition, the State will begin paying for deferred mandates over five years, starting in FY 2006-07.

In addition, the agreement would place in the Constitution existing statutory provisions requiring the pay back of the VLF "gap" loan in FY 2006-07, guaranteeing replacement property taxes for the sales taxes being used to pay for the Proposition 57 Fiscal Recovery Bond, reestablishing local government's authority to impose a 1 percent sales tax rate after the Bond is paid, and establishing the five-year payback of deferred mandates.

The LAO's Concerns

While noting that the proposed agreement will provide the State with budget savings and local governments with financial stability, while improving accountability in the mandate process, the LAO has major concerns with each of the elements of the proposed agreement.

- The constitutional protection of local revenues will lock in place the existing local finance system, preventing the Legislature from making changes to protect local revenues, as they did after Proposition 13, or implementing reforms such as the reallocation of local sales taxes or the "AB 8" allocation of property taxes to

reflect new needs or changed realities, or lowering the sales tax rate in exchange for a broadening of the sales tax base.

- The swap of VLF revenues for property taxes is extremely complex but does not appear to have a persuasive policy rationale since concerns about future State payment of VLF backfill payments could be more simply eased by putting the requirement to pay backfill into the Constitution. Moreover, the hope that heavier reliance on property taxes will encourage local governments to promote housing rather than retail development is not very persuasive since the VLF revenue being surrendered is distributed on a per-capita basis and should have already been an incentive for housing.
- The agreement only provides the State with short-term budget relief (and possibly longer-term cost increases) whereas it really needs longer-term and permanent relief to solve its structural budget deficit. At the same time, many local governments will have to reduce services and/or increase fees during the two years their property taxes are reduced.
- While the proposed changes regarding State mandates would improve the process, the LAO is concerned about the complications of having a dual process with a fast track for local government mandates, and a slower process for education mandates. The LAO also questions why employee benefit-related mandates are exempt from the automatic sunset, worries that the expedited mandate determination process could result in decisions that fail to meet the legal standards of courts, and believes that the Controller, not the Department of Finance, should have the difficult and controversial responsibility of estimating mandate costs since the latter has a conflict of interest. In addition, the LAO notes that the broadened definition of a mandate to include increased share of cost will make it more difficult, in the future, to realign fiscal and program responsibilities for jointly financed programs.

The LAO's Alternative

Given its concerns, the LAO has suggested that the Legislature consider changes to the local agreement as it acts on the constitutional amendment and statutory changes required to implement the agreement.

- In order to maintain State authority over local finance while protecting local revenues from being taken by the State, the LAO recommends that "the Legislature consider policies that protect local revenue streams in the *aggregate*, yet maintain authority to alter these taxes and the allocation of these revenues among local governments."

- In the absence of a more compelling policy rationale, the LAO recommends that the Legislature reject the swap of VLF for property taxes, and instead amend the Constitution to guarantee the annual VLF backfill to local governments.
- In order to alter the burden of the local contribution to the State budget and provide relief over a longer period of time, the LAO proposes a very different way of achieving \$2.6 billion in local government reductions. The LAO would retain the Administration's proposed \$250 million two-year shift from redevelopment agencies, shift \$220 million in property taxes from special districts on a permanent basis, determined by county boards of supervisors; eliminate two subventions, the Citizens' Option for Public Safety and the Juvenile Justice Grant programs, to save \$200 million, and spread the VLF gap loan repayment over three years instead of a lump sum payment of \$1.2 billion in FY 2006-07. Cities and counties, whose discretionary revenue would not be affected, would lose their share of the eliminated subventions.
- While retaining some of the key elements of the Agreement's mandate proposal, in particular the automatic sunset requirement and the repeal of the Legislature's ability to suspend mandates, the LAO's proposal would go much further to cover all mandates, assign responsibility for cost estimates to the Controller (with assistance from a local agency advisory board), and suggest an alternative way of determining a reimbursement methodology.

The LAO concludes by urging the Legislature to modify the Local Government Agreement along the lines that they have recommended to bring it into "greater alignment with legislative goals and state fiscal objectives." It remains to be seen whether and how much of their advice will be taken when the Legislature takes up the Agreement.

Status of County-Interest Legislation

County-supported AB 340 (Frommer), which would make it illegal to sell, offer for sale, buy, possess, manufacture, or distribute Mobile Infrared Transmitters that are capable of changing the sequence of a traffic signal, was amended on May 24, 2004 to exclude a public transit passenger vehicle from this prohibition, make it an infraction to install such a device, and delete the possession of two or more of these devices as a misdemeanor. AB 340 remains in the Senate Transportation Committee.

County-opposed AB 2013 (Steinberg), which would repeal the requirement for statewide fingerprint imaging to determine eligibility for CalWORKs and Food Stamps, and make conforming changes to the Kin-GAP Program, passed the Assembly on May 20, 2004 by a vote of 41 to 33. This measure is currently at the Senate Desk awaiting referral to a policy committee.

Each Supervisor
May 25, 2004
Page 5

County-supported AB 2783 (Simitian), which would allow counties the option to increase recording fees on real estate documents up to \$2 to fund programs to deter, investigate, and prosecute civil proceedings involving the financial abuse of elder and dependent adults through fraudulent real estate transactions, passed the Assembly on May 24, 2004, by a vote of 41 to 32. This measure is currently at the Senate Desk awaiting referral to a policy committee.

County-sponsored AB 2857 (Laird), which would protect public agencies from losing tax revenue, and ensure that taxpayers are not barred from an appropriate administrative reduction in assessments due to a decline in value, passed the Assembly on May 20, 2004 by a vote of 47 to 29. This measure is currently at the Senate Desk awaiting referral to a policy committee.

County support and amend SB 1375 (Scott), which would authorize the California Transportation Commission to relinquish a portion of State Highway Route 164 to the County of Los Angeles to allow the County to make improvements to Rosemead Boulevard, passed the Assembly Appropriations Committee on May 20, 2004 by a vote of 10 to 0, and will now go to the Assembly Floor.

County-opposed SB 1462 (Kuehl), which would require the lead agency of any project located beneath special use airspace that would adversely affect military flights, to transmit all environmental documents to the State Office of Planning and Research, which will send the documents to the appropriate military organization, passed the Senate Appropriations Committee on May 20, 2004 by a vote of 8 to 4, and will now go to the Senate Floor.

We will continue to keep you advised.

DEJ:GK
MAL:JF:JR:EW:JL:MS:ib

c: Executive Officer, Board of Supervisors
 County Counsel
 Local 660
 All Department Heads
 Legislative Strategist
 Coalition of County Unions
 California Contract Cities Association
 Independent Cities Association
 League of California Cities
 City Managers Associations
 Buddy Program Participants